

Message Text

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ACTION EA-09

INFO OCT-01 ISO-00 AID-05 CIAE-00 COME-00 EB-07 FRB-01

INR-07 NSAE-00 USIA-15 XMB-04 OPIC-06 SP-02 CIEP-02

LAB-04 SIL-01 OMB-01 NSC-05 SS-15 STR-04 CEA-01 EAE-00

FEAE-00 ERDA-07 FPC-01 DOTE-00 OES-06 PA-02 PRS-01

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P 300920Z JUL 76

FM AMEMBASSY TOKYO

TO TREASURY DEPT WASHDC PRIORITY

SECSTATE WASHDC PRIORITY 1247

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TREASURY FOR SYVRUD AND FAUVER

E.O. 11652: N/A

TAGS: EFIN, JA

SUBJECT: INFLATION OUTLOOK FOR JAPAN

1. SUMMARY: SERIOUS INFLATIONARY PRESSURES PERSIST IN JAPAN AND APPEAR TO BE ACCELERATING. HEAVY INDUSTRY IS SEEKING FURTHER PRICE HIKES, WHICH WOULD PUSH UP WPI, AND INCREASES FOR PUBLICLY REGULATED PRICES WILL RAISE CPI. BY DEC 1976 YEAR-OVER-YEAR INCREASE IN WPI LIKELY TO BE ABOVE 9 PERCENT, AND YEAR-OVER-YEAR RISE IN CPI WILL BE ABOVE 10 PERCENT. END SUMMARY.

2. THE PROBLEM OF JAPAN'S CONTINUING INFLATION, ESPECIALLY THE ACCELERATING INFLATION AT THE WHOLESALE PRICE LEVEL, IS RECEIVING INCREASED ATTENTION FROM GOJ OFFICIALS. DURING THE FIRST SIX MONTHS (DEC 76-JUNE 76), WPI ROSE AT 7.3 PERCENT ANNUAL RATE. THERE IS LITTLE PROSPECT THAT INFLATIONARY PRESSURES WILL BE EASE IN THE NEAR FUTURE. SEVERAL INCREASES IN PUBLICLY REGULATED PRICES HAVE OCCURRED

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RECENTLY OR ARE SCHEDULED FOR THE LATTER HALF OF THIS

YEAR. RATES FOR FOUR MAJOR ELECTRIC POWER COMPANIES WERE RAISED AN AVERAGE OF 27 PERCENT IN JUNE AND INCREASES FOR OTHER ELECTRIC POWER COMPANIES ARE SCHEDULED FOR OCTOBER; THE PRODUCERS' PRICE FOR RICE WAS RAISED AN AVERAGE OF 7.3 PERCENT IN JULY, AND RAILWAY FEES WILL GO UP ABOUT 50 PERCENT IF THE DIET APPROVES MOF RECOMMENDATION TO INCREASE FARES. AT THE SAME TIME, FIRMS IN SUCH BASIC INDUSTRIES AS PETROLEUM REFINING AND IRON AND STEEL ARE ATTEMPTING TO RAISE THEIR PRICES IN ORDER TO COVER INCREASED COSTS OF MATERIAL AND WAGES AND IMPROVE THEIR PROFIT POSITION. STEEL COMPANIES' REQUEST FOR YEN10,000 PER TON PRICE INCREASE IS STILL BEING OPPOSED BY AUTO MAKERS BUT HAS BEEN AGREED TO BY MAJOR ELECTRIC APPLIANCE MANUFACTURERS.

3. CONSUMER PRICES HAVE ALSO FAILED TO CALM DOWN AND THE TOKYO CPI ROSE AT A 14.2 PERCENT ANNUAL RATE DURING THE FIRST SIX MONTHS OF THIS YEAR. SINCE MAJOR IMPACT OF INCREASES IN REGULATED PRICES WILL BE ON CPI, THERE APPEARS TO BE LITTLE PROSPECT FOR ANY EASING OF INFLATIONARY PRESSURES THIS YEAR. IF THE RENEWED ACCELERATION OF WHOLESALE PRICES IS MAINTAINED THROUGH THE LATTER HALF OF 1976 THIS DEVELOPMENT WOULD VERY PROBABLY PLACE STRONG UPWAR

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4. FOLLOWING TABLE SHOWS QUARTERLY INCREASES IN WHOLESALE AND CONSUMER PRICE INDICES DURING 1975 AND 1976 AND MONTHLY INCREASES IN 1976. FIGURES IN PAREN INDICATE INCREASE IN THE INDEX RELATIVE TO THE SAME MONTH OF THE PRIOR YEAR.

	WPI	CPI-TOKYO
(1970-100; JEI 471)		
QUARTERLY DATA, 1975-1976:		
1975 I	MIN 0.6	1.5
II	MIN 0.2	4.0
III	0.6	0.9
IV	1.1	2.4

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1976 I	1.9	2.5
II	1.6	3.3
MONTHLY DATA FOR 1976:		
1976 JAN	0.8 (2.4)	0.3 (10.2)
FEB	0.7 (3.7)	0.7 (10.5)
MAR	0.6 (4.5)	0.5 (9.9)
APR	0.5 (4.9)	2.5 (10.0)
MAY	0.4 (5.3)	MIN 0.1 (8.7)

JUNE	0.5 (5.9)	0.9 (9.7)
JULY	1.0 (5.9)E	0.0 (9.4)

NOTE: E- ESTIMATE BASED ON DATA FOR JULY 1-20.

5. THERE ARE SEVERAL SOURCES OF UPWARD PRESSURE ON THE WPI:

A. HIGHER PRICES FOR IMPORTED RAW MATERIALS HAVE BEGUN TO HAVE SOME IMPACT ON JAPAN'S WPI ALTHOUGH THIS HAS OFFSET TO SOME DEGREE BY MODEST APPRECIATION OF THE YEN SINCE BEGINING OF THIS YEAR. GOJ OFFICIALS DO NOT THINK RISING COMMODITY PRICES WILL CAUSE A REPEAT OF THE WPI "EXPLOSION" OF 1973 AND 1974.

NOTE BY OC/T: OMISSION CORRECTION TO FOLLOW.

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B. THE SUDDEN ACCELERATION IN ECONOMIC RECOVERY IN EARLY 1976 RESULTED IN PRICE INCREASES IN CERTAIN MANUFACTURED COMMODITIES, INCLUDING MACHINERY, ACCORDING TO ONE KNOWLEDGEABLE EPA OFFICIAL. HOWEVER, OFFICIAL ANTICIPATES SOME SLOWING OF THE PACE OF RECOVERY LATER THIS YEAR WITH FEWER PRICE INCREASES SO AS TO ALLOW PRODUCTIVITY INCREASES AND DECLINING UNIT LABOR COSTS NORMALLY ASSOCIATED WITH

JAPAN'S RECOVERY PROCESS TO EASE INFLATIONARY PRESSURES.

C. GOJ APPROVED PRODUCTION RESTRAINTS IN SUCH BASIC INDUSTRIES AS PETROLEUMREFINING, CHEMICALS, CEMENT AND IRON AND STEEL APPEAR TO HAVE CONTRIBUTED TO INCREASED WHOLESALE PRICES DURING THE FIRST HALF OF 1976. EPA OFFICIALS SAYS THAT ALL FORMAL PRODUCTION RESTRAINTS HAVE NOW BEEN REMOVED, WHICH WILL HELP PREVENT FURTHER PRICE INCREASES IN THESE INDUSTRIES.

6. CONCERN ABOUT WHOLESALE PRICE OUTLOOK IS STRONGEST AT BOJ, WHICH COLLECTS WHOLESALE PRICE DATA AND CONSIDERS ITSELF RESPONSIBLE FOR MAINTAINING STABILITY IN WHOLESALE PRICES. BOJ OFFICIALS SAY MOF AND EPA SHARE THEIR CONCERN.
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NEVERTHELESS, EPA WAS DESCRIBED AS CONCERNED THAT A SHIFT AT THIS TIME TO A POLICY OF TIGHT MONEY TO CURB INFLATION MIGHT CHOKE OFF CURENT RECOVERY. BOJ OFFICIAL SAID MITI CONTIUES TO SUPPORT INTERESTS OF SPECIFIC JAPANESE INDUSTRES AND HAS SHOWN LITTLE SYMPATHY TO BOJ COMPLAINTS ABOUT RECENT WHOLESALE PRICE TRENDS.

7. AVERAGE LEVEL OF WHOLESALE PRICE INDEX IN CY 1976 WILL BE ABOUT 6.5 PERCENT ABOVE WPI FOR CY 1975. HOWEVER, DEGREE OF MOVEMENT WITHIN CY 1976 WILL DEPEND HEAVILY UPON DEVELOP-
METS AFTERJULY. IF PACE OF INCREASE IN WPI DURING LATER HAL OF THIS YEAR IS NO GREATER THAN FOR JAN-JUNE PERIOD, YEAR-TO-YEAR RISE BY DEC 1976 WILL BE PERHAPS 7.3 PERCENT. HOWEVER, DATA FOR FIRST 20 DAY OF JULY INDICATE THAT MONTHLY INCREASEIN FULL MONTH WILL BE ABOUT 1 PERCENT AND CLOSE TO WHAT BOJ OFFICIAL DESCRIBED AS FLASHPOINT THAT COULD IGNITE SERIOUS INFLATIONAY EXPECTATIONS. IF WPI INCREASES AT 1 PERCENT PER MONTH THROUGH LATTER ALF OF THIS YEAR, THEN YEAR-TO-YEAR RISE BY DEC 1976 WILL BE 9.9 PERCENT. IN VIEW OF CONTINUING PRESSURES FROM INTL COMMODITY PRICES, AS WELL AS LIKELIHOOD OF SOME PRICE INCREASES IN HEAVY INDUSTRY, YEAR-TO-YEAR INCREASE IN WPI IN FINAL MONTH OF THIS YAR WILL PROBABLY BE MORE THAN 8 PERCENT AND QUITE POSSIBLY IN 9-10 PERCENT RAGE.

8. INCREASES IN PUBLICILY REGULATED PRICES WILL KEEP UPWARD PRESSURE ON CPI. EPA ESTIMATES THAT THE 10.3 PERCENT INCREASE IN CONSUMERS PRICE OF RICE, JUST ANNOUNCED, WILL RAISE CPI BY 0.4 PERCENT. PLANNED INCREASES IN RAILWAY FEES WOULD BOOST CPI ANOTHER 0.5 PERCENT. THERE WILL BE THE USUAL DELAYED BUT ADDITIONAL PRESSURES FROM PAST INCREASES IN WPI WHICH, UNLIKE A YEAR AGO, HAS NOW BEEN INCREASING PERSISTENTLY IN EACH OF THE LAST 12 MONTHS. ALL OF THESE POINT TO LARGER INCREASES IN

CPI IN THE PERIOD AHEAD THAN IN THE PAST YEAR.
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